



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Memorandum

Date AUG 27 1998
From June Gibbs Brown
Inspector General
Subject Audit of Medical Supply Ancillary Costs Claimed by 31 Skilled Nursing Facilities Owned by Horizon West, Inc. (A-09-98-00060)
To Nancy-Ann Min DeParle
Administrator
Health Care Financing Administration

This memorandum is to alert you to the issuance on August 31, 1998, of our final report. A copy is attached.

We found \$1,915,365 of the \$2,405,056 claimed as ancillary medical supplies by Horizon West, Inc. (Horizon) for Fiscal Year Ended (FYE) June 30, 1991 was misclassified. The costs should have been claimed as other types of costs, such as routine, dietary, and administrative and general costs. As a result, Horizon was overpaid \$1,076,338 by Medicare.

On June 23, 1998, Horizon voluntarily repaid the Federal Government \$1,697,662. This amount included the \$1,076,338 we identified as an overpayment plus an additional \$621,324 to cover our estimate of overpayments made for FYE 1992 through 1995. Negotiations are continuing among Federal Government representatives and the provider for possible additional repayments to the Medicare program.

Because Horizon currently has a different fiscal intermediary, we had no procedural recommendations on monitoring Horizon's operations in this report which is directed to Mutual of Omaha for needed financial adjustments. A separate report with any procedural recommendations needed to monitor Horizon will be issued to the current fiscal intermediary, Blue Cross of California.

Any questions or comments on any aspect of this memorandum are welcome. For further information, contact:

Mr. Lawrence Frelot
Regional Inspector General
for Audit Services, Region IX
(415) 437-8360

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**AUDIT OF MEDICAL SUPPLY
ANCILLARY COSTS CLAIMED BY
31 SKILLED NURSING FACILITIES
OWNED BY HORIZON WEST, INC.**



JUNE GIBBS BROWN
Inspector General

AUGUST 1998
A-09-98-00060



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Region IX
Office of Audit Services
50 United Nations Plaza
San Francisco, CA 94 102

CIN: A-09-98-00060

Mr. Scott J. Manning
First Vice President
Audit and Reimbursement
Mutual of Omaha Insurance Company
P. O. Box 1604
Omaha, Nebraska 68101

Dear Mr. Manning:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of Inspector General, Office of Audit Services (OAS) report entitled "AUDIT OF MEDICAL SUPPLY ANCILLARY COSTS CLAIMED BY 31 SKILLED NURSING FACILITIES OWNED BY HORIZON WEST, INC."

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed as well as other conclusions and recommendations in this report represent the findings and opinions of the HHS/OIG/OAS. Final determination on these matters will be made by authorized officials of the HHS operating divisions.

This report and any finding of overpayments herein in no way addresses whether or not there are facts or legal bases to support a criminal, civil or administrative action under applicable criminal statutes or other authorities, such as the federal civil False Claims Act, the Program Fraud Civil Remedies Act, or the Civil Monetary Penalties Law. Nor does this report in any way conclude or suggest that the proper disposition of matters discussed herein is through administrative recoupment only.

Page 2 - Scott J. Manning

Should you have any questions or comments concerning the matters commented on in this report, please direct them to the HHS official named below.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

To facilitate identification, please refer to Common Identification Number A-09-98-00060 in all correspondence relating to this report.

Sincerely yours,

A handwritten signature in cursive script, reading "Lawrence Frelot".

Lawrence Frelot
Regional Inspector General
for Audit Services

Enclosures

Direct Reply to HHS Official:

Mr. Carl Hawkins
Associate Regional Administrator for Medicare
Health Care Financing Administration
Region VII
601 East 12th Street, Room 242
Kansas City, Missouri 64106

EXECUTIVE SUMMARY

BACKGROUND

As part of Operation Restore Trust, a departmental initiative to combat fraud, waste, and abuse, the Office of Inspector General (OIG) identified skilled nursing facilities (**SNFs**) that had aberrant patterns of claims for ancillary medical supplies (i.e., medical supplies not included in patients' daily routine care). This report presents the results of our audit of the ancillary medical supplies claimed by Horizon West, Inc. (Horizon), a corporation owning and operating 31 **SNFs** in California, for the Fiscal Year Ended (FYE) **June 30, 1991**. Because of the involvement of several other Federal agencies relative to the audit findings, Horizon has offered estimated **financial** adjustment payments to the Health Care Financing Administration (HCFA) that, if accepted, will cover Medicare overpayments through 1995.

OBJECTIVE

The objective of our audit was to determine if the costs claimed as ancillary medical supplies during FYE June 30, 1991 were allowable, reasonable, and allocable under Medicare rules.

SUMMARY OF FINDINGS

We found that \$1,915,365, or 80 percent, of the \$2,405,056 claimed ~~as~~ ancillary medical supplies by Horizon was misclassified. The \$1,915,365 should have been claimed as routine costs (\$1,459,515), dietary costs (\$293,867), and administrative and general costs (\$161,983). As a result of the misclassification, Horizon was overpaid \$1,076,338 according to calculations by the Medicare fiscal intermediary, Mutual of Omaha.

The inappropriate ancillary costs included:

- Medical personnel (\$866,297),
- Miscellaneous routine items (\$593,218),
- Food products (\$293,867),
- Infectious waste removal (\$67,772),
- Consultant fees (\$63,176), and
- Computers and software (\$31,035).

The costs were not allowable as ancillary because they did not meet the specific requirements of Medicare cost principles as published in HCFA's Provider Reimbursement Manual.

A Horizon representative told us that it included the costs as ancillary because a consultant advised the organization that it was appropriate to do so, had been previously allowed by another fiscal intermediary for other SNFs, and would increase the company's Medicare revenue.

CONCLUSION

In our draft report, we recommended that Mutual of Omaha reclassify the routine costs that we identified and disallow \$90,510 as unsupported costs. In its response to our draft report, Horizon agreed with our findings and recommendations, except for the \$90,510 in unsupported costs. It subsequently provided adequate support to classify the \$90,510 as additional routine costs.

On June 23, 1998, Horizon voluntarily repaid the Federal Government \$1,697,662. This amount included the \$1,076,338 we identified as an overpayment plus an additional \$621,324 to cover estimated overpayments made for Fiscal Years 1992 through 1995.

Effective July 1, 1993, Mutual of Omaha is no longer the fiscal intermediary for Horizon's SNFs. Therefore, we are not making any procedural recommendations to Mutual of Omaha relative to this provider in this report. A separate report with procedural recommendations on monitoring Horizon's operations will be issued to the current fiscal intermediary, Blue Cross of California.

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- Appendix A: Summary of Findings by Facility
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INTRODUCTION

BACKGROUND

**Horizon West,
Inc.**

Horizon is a for-profit corporation located in Rocklin, California. During its FYE June 30, 1991, it owned 31 SNFs throughout California. These 31 SNFs reported about \$68 million in total costs during that year, and the Medicare program reimbursed them about \$5.6 million for their costs of caring for Medicare patients. Of the \$68 million, Horizon claimed about \$2.4 million as ancillary medical supply costs.

Horizon purchased medical supply goods and services for all its SNFs, issued checks to pay for those goods and services, and maintained an accounting system that classified costs by facility.

**Operation
Restore Trust**

As part of the Department of Health and Human Services' efforts to combat fraud, waste, and abuse, the OIG, in partnership with HCFA and the Administration on Aging, undertook an initiative called Operation Restore Trust. This project was designed to specifically target Medicare and Medicaid abuse and misuse in nursing home care, home health care, and durable medical equipment because they are three of the fastest growing areas in Medicare.

The OIG's audit of Horizon's 31 SNFs is one of several conducted in a national review of ancillary medical supplies. States included in this review are California, Florida, Illinois, New York, and Texas.

The 31 SNFs owned by Horizon were selected by the OIG for this audit because some of them had significantly higher medical supply costs than comparable SNFs.

**Medicare
Reimbursement
Principles**

During the period of our audit, Medicare generally reimbursed SNFs on a reasonable cost basis as determined under principles established in the law and regulations. In order to determine their reasonable costs, providers are required to submit cost reports annually, with the reporting period based on the provider's fiscal accounting year. The SNFs are paid on an interim basis, and the cost report is used to

arrive at a final settlement amount. Costs are classified on the cost report as either routine or ancillary.

Routine services are generally those services included by the provider in a daily service--sometimes called the "room and board" charge. Included in routine services are the regular room, dietary and nursing services, minor medical and surgical supplies, and the use of certain equipment and facilities for which a separate charge is not customarily made.

According to Medicare rules, "...the following types of items and services... are always considered routine in an SNF for purposes of Medicare cost apportionment, even if customarily considered ancillary by an SNF:

- "o All general nursing services, including administration of oxygen and related medications. . .handfeeding. **incontinency** care, tray service, enemas, etc.

- "o Items which are furnished routinely and relatively uniformly to all patients, e.g., patient gowns, paper tissues, water pitchers, basins, bed pans, deodorants, mouthwashes.

- "o Items stocked at nursing stations or on the floor in gross supply and distributed or utilized individually in small quantities, e.g., alcohol, applicators, cotton balls, bandaids, antacid, aspirin, (and other nonlegend drugs ordinarily kept on hand), **suppositories**, tongue depressors.

- "o Items which are utilized by individual patients but which are reusable and expected to be available in an institution providing an SNF level of care, e.g., ice bags, bed rails, canes, crutches, walkers, wheelchairs, traction equipment, other durable medical equipment (DME) which does not meet the criteria for ancillary services in **SNFs** under **§2203.2**, and the requirements for recognition of ancillary charges under **§2203.....**

- "o Special dietary supplements used for tube feeding or oral feeding, such as elemental high nitrogen diet, even if written as a prescription item by a **physician....**" (**Provider Reimbursement Manual**, section 2203.1)

Ancillary services are those services directly identifiable to individual patients, such as laboratory, radiology, drugs, , medical supplies, and therapies. Section 2203.2 of the **Provider Reimbursement Manual**, effective during our audit period,

specified that certain items and services could be considered ancillary if they met each of the following three requirements:

- "0 direct identifiable services to individual patients, and
- "0 furnished at the direction of a physician because of specific medical needs, and
- "o one of the following:
 - Not reusable - e.g., artificial limbs and organs, braces, intravenous fluids or solutions, oxygen (including medications), disposable catheters;
 - Represent a cost for each preparation, e.g., catheters and related equipment, colostomy bags, drainage equipment, trays and tubing; or
 - Complex medical equipment - e.g., ventilators, intermittent positive pressure breathing (IPPB) machines, nebulizers, suction pumps, continuous positive airway pressure (CPAP) devices, and bead beds such as air fluidized **beds**."

Medicare pays its portion of a provider's reasonable costs based upon an apportionment between program beneficiaries and other patients so that Medicare's share of the costs is based on services received by Medicare beneficiaries. For routine costs, Medicare's share is determined on the basis of a ratio of Medicare patient days to total patient days. For ancillary costs, Medicare's share is determined on the basis of the ratio of total covered beneficiary charges for ancillary services to total patient charges for such services.

Classifying costs as ancillary rather than as routine can result in higher Medicare **reimbursement** to **SNFs** because of two factors. First, **SNFs** generally have higher Medicare utilization for ancillary services than for routine services. That is, Medicare eligible patients generally receive more ancillary services than other patients but comprise a smaller portion of the total number of patients. Thus, Medicare's share of ancillary costs is usually greater than its share of routine costs. Second, Federal law (specifically, section 1888 of the Social Security Act) limits Medicare reimbursement for **SNFs'** routine costs to 112 percent of the mean operating costs of other similar **SNFs**. Thus, Medicare does not share in routine costs exceeding the Federal limit, unless the provider applies for and receives an exception from HCFA.

**Administration
of Medicare**

The HCFA administers the Medicare program and designates certain fiscal intermediaries to perform various functions, such as processing Medicare claims, performing audits, and providing consultative services to assist SNFs as providers. Mutual of Omaha served as the fiscal intermediary for Horizon's SNFs during the FYE June 30, 1991.

OBJECTIVE, SCOPE, and METHODOLOGY

The objective of our audit was to determine if the costs claimed (\$2,405,056) as ancillary medical supplies during FYE June 30, 1991 by the 31 SNFs owned by Horizon were allowable, reasonable, and allocable under Medicare rules.

Medicare cost reports are subject to audit. In 1992, Mutual of Omaha performed limited scope desk reviews of Horizon's SNFs cost reports for FYE June 30, 1991 and made adjustments to the reported costs. The \$2,405,056 of ancillary medical supply costs are the net costs after adjustments made by Mutual of Omaha to arrive at Horizon's 31 amended cost reports.

Twenty-seven of the 31 SNFs had cost reports covering the entire 12-month period ended June 30, 1991. Four facilities had shorter periods for their cost reports:

- Delta Convalescent Hospital's cost report covered 11 months (July 1, 1990 through May 31, 1991) because it was sold effective June 1, 1991.
- Katherine Convalescent Hospital's cost report covered 10 months (July 1, 1990 through April 30, 1991) because it was sold effective May 1, 1991.
- Placerville Pines Convalescent Hospital's cost report covered 6 months (January 1, 1991 through June 30, 1991) because it changed its fiscal year effective January 1, 1991.
- South Gate Care Center's cost report covered only 6 months because it was purchased by Horizon effective January 1, 1991.

To accomplish our objective, we traced the costs claimed for ancillary medical supplies on Horizon's 31 amended cost reports to its accounting records. For accounts 810039 (ancillary-professional services), 810020 (ancillary-employee benefits), and 810065 (ancillary-purchased services), we reviewed journal entries to the accounting records, discussed the nature of the costs with Horizon's staff, and reviewed other supporting documentation.

For all other costs claimed (accounts 810044 [patient supply expenses-medical care material] and 850644 [oxygen expenses medical care supply]), we traced the costs from the accounting records to individual invoices, examined each invoice to determine specifically what items and services were purchased, and then determined if the costs were properly classified as ancillary. Because overpayments were required to be determined for each SNF individually, we considered it more efficient and practical to examine all invoices rather than a sample of invoice from each facility.

We discussed many of the specific items purchased by Horizon with Mutual of Omaha's auditors and medical review staff to determine their allowability as ancillary medical supplies. We also had discussions with Horizon's staff regarding the company's accounting policies and procedures and its claiming of costs on the Medicare cost reports.

Because of the complexity of determining Medicare reimbursement, we requested that Mutual of Omaha calculate the impact of the unallowable costs that we identified. It used proprietary software to perform this calculation. We did not verify that the overpayment that Mutual of Omaha calculated was accurate.

We conducted our audit in accordance with generally accepted government auditing standards. The fieldwork was performed at Horizon West, Inc. in Rocklin, California between August 1995 and May 1996. Subsequent to the issuance of our draft report, dated August 30, 1996, Horizon contested to Mutual of Omaha the classification of 46 items as routine. Mutual of Omaha's medical review staff agreed with Horizon that 32 of the 46 items were ancillary, and, as a result, we performed additional fieldwork in March 1997 to redetermine the financial impact of the 32 items. In addition, subsequent to the issuance of our draft report, we have been coordinating and cooperating with other Federal agencies reviewing our Horizon West, Inc. audit results.

FINDINGS AND CONCLUSION

Of the \$2,405,056 claimed as ancillary medical supplies by Horizon's 31 SNFs, we identified \$1,915,365, or 80 percent, that had been misclassified. These costs were allowable, however, as routine costs (\$1,459,515), dietary costs (\$293,867), and administrative and general costs (\$161,983) (see Appendix A for a breakdown of these costs by individual SNF).

The unallowable costs as claimed and as audited are shown in the table below. The remaining 20 percent, or \$489,691, was allowable as ancillary costs.

	Claimed as Ancillary	-Allowable as-		
		Routine	Dietary	A & G
Medical personnel	\$866,297	\$866,297		
Miscellaneous routine items	593,218	593,218		
Food products	293,867		\$293,867	
Infectious waste removal	67,772			\$67,772
Consultant fees	63,176			63,176
Computers and software	31,035			31,035
Totals	\$1,915,365	\$1,459,515	\$293,867	\$161,983

By classifying the costs as ancillary, Horizon was able to significantly increase its Medicare reimbursement. According to Mutual of Omaha, the misclassification of the \$1,915,365 as ancillary medical supplies resulted in Horizon's 31 SNFs being overpaid by \$1,076,338.

Under Medicare's rules, costs for medical supply items and services furnished routinely to all patients should **always be** considered as routine costs. In order to be classified as an ancillary cost, the item or service must be directly identifiable to an individual patient, be furnished at the direction of a physician because of special medical needs, and be either not reusable, represent a cost for each preparation, or complex medical equipment.

The costs we identified were for items or services that did not meet these specific requirements for treatment as ancillary medical supplies. In some cases, the costs should have been treated as dietary costs or as administrative and general costs.

According to documents we obtained at Horizon, the company hired a consultant in January 1990. The consultant, in addition to other services provided, developed a plan, called the "**revenue enhancement program," to increase the **SNF's** Medicare revenue by changing the way certain medical supply costs were classified. According to Horizon staff, the company adopted this new program, in part, because the consultant advised the organization that the changes were appropriate, had been previously allowed by another fiscal intermediary (not Mutual of Omaha) for other **SNFs**, and would increase the company's revenue.

Medical Personnel

We found \$866,297 in medical personnel costs that were included as ancillary medical supplies. These costs consisted of \$726,748 for contracted nursing services and \$139,549 for costs of other medical personnel.

Horizon had claimed a portion of the salaries and benefits of its employee nurses and contracted nurses as ancillary medical supplies in its cost reports for FYE 1991 through 1993. The costs of the nursing services, according to Horizon staff, represented an allocation to ancillary medical supplies of part of their compensation based upon a time study that Horizon conducted. Horizon believed that the nursing costs could be claimed as ancillary because the time spent was related to the administration of ancillary medical supplies, such as the time a nurse spent to install a catheter, a proper ancillary item.

However, each year Mutual of Omaha auditors would reclassify the costs to routine and advise Horizon that the costs did not qualify as ancillary. The HCFA advised Horizon in a letter, dated June 3, 1993, that nursing salaries were not ancillary because they did not meet one of the required elements of section 2203.2 of the Provider Reimbursement Manual, namely the salaries did not represent an item that was "not reusable," did not have a separate cost for each preparation, or were not complex medical equipment (see page 3 of this report). Horizon appealed the issue to the Provider Reimbursement Review Board and continued to include the costs each year.

Although Mutual of Omaha's auditors identified and reclassified all of the allocated costs for the employee nurses from several of Horizon's ancillary medical supply accounts for FYE June 30, 1991, it did not identify the costs for contracted nurses that were contained in account 810039 and, for two **SNFs**, amounts

contained in account 810020. Thus, the \$726,748 should now be reclassified to routine.

The \$139,549 in other medical personnel costs was an allocated portion of the total compensation for each SNFs' medical director, pharmacy consultant, and medical records clerk. These costs also should have been treated as routine.

**Miscellaneous
Routine Items**

Our review of vendor invoices identified \$593,218 of various miscellaneous items that had been inappropriately classified as ancillary costs.

The more significant routine items included \$141,257 in incontinent supplies, \$62,706 in latex gloves, \$51,009 in adhesive bandages, and \$28,675 in general purpose ointments.

According to the Medicare rules (provider Reimbursement Manual, section 2203.1), these types of items are always to be considered routine in a SNF.

Food Products

We identified \$293,867 in food products that should have been claimed as dietary costs. This amount included \$259,707 for enteral food (liquid nutrition supplements) and \$34,160 for common grocery food items.

Enteral food is liquid nourishment administered orally to patients who cannot ingest an appropriate amount of calories to maintain an acceptable nutritional status. Horizon purchased enteral food products under various brand names, such as Ensure, Osmolite, and Vitaneed. Special dietary supplements are specifically listed in section 2203.1 of the Provider Reimbursement Manual as items that are always considered routine in a SNF even if prescribed by a physician.

The grocery items included milk products, vinegar, flavored food extracts, strawberry shake nutritional supplements, distilled water, and Gatorade. These items do not meet the criteria of ancillary medical supplies and should have been classified as dietary costs.

**Infectious
Waste Removal**

We also identified \$67,772 in unallowable ancillary costs for removal of infectious waste material. The costs included expenses for disposal services performed by private companies, purchases of special containers, and purchases of infectious waste liners.

These costs should have been classified on the cost reports as administrative and general costs.

Consultant Fees

We identified \$63,176 in consultant fees that were claimed as ancillary costs. Horizon paid these fees to a consultant who advised the company about a variety of matters, including Medicare billing procedures at individual SNFs and strategies on how to improve its revenue from Medicare. The costs should have been classified as administrative and **general costs**, not as ancillary costs.

Computers and Software

Horizon inappropriately classified \$31,035 in computer related costs as ancillary **medical supplies**. The costs, which were included in account 810065 (purchased services), were monthly payments for 13 desktop computers, various software programs, and computer maintenance support that was purchased in October of 1989.

Expenditures for computer related equipment and services do not qualify as ancillary medical supply items under Medicare's rules. Therefore, the \$31,035 should be reclassified as administrative and general costs.

Conclusion

Horizon claimed ancillary medical supply costs totaling about \$2.4 million for the FYE June 30, 1991 for the 31 **SNFs** it owned in that period. Based upon our review, we considered **\$1,915,365** of those costs to be unallowable as ancillary costs under Medicare cost reimbursement principles.

According to calculations by staff at Mutual of Omaha, the 31 **SNFs** owned by Horizon were overpaid **\$1,076,338** by Medicare as a result of the unallowable costs we identified.

We recommended in our draft report, issued August 30, 1996, that Mutual of Omaha reclassify the routine costs that we identified and disallow \$90,510 as unsupported costs.

Horizon's Comments

In its response to our draft report (see Appendix B), Horizon agreed with our findings and recommendation, except for the \$90,510 in unsupported costs. It subsequently provided adequate support to classify the \$90,510 as additional routine costs.

OIG's Comments

On June 23, 1998, Horizon voluntarily repaid the Federal Government \$1,697,662 representing the amount identified by our audit as an overpayment (\$1,076,338) plus an additional \$621,324 to cover our estimate of overpayments made for Fiscal Years 1992 through 1995.

In this report, we are not making any procedural recommendations to Mutual of Omaha because it is no longer the fiscal intermediary for any of Horizon's SNFs. We plan on issuing a separate report on the need for any procedural recommendations to Horizon's current fiscal intermediary, Blue Cross of California.

APPENDICES

Provider Name	Provider Number	Costs Claimed	IMMEDIATELY CLASSIFIED COSTS						Total	Over-payment
			Medical Personnel	Consulting	Misc. Med. Supplies	Food Products	Waste Removal	Computers		
Arlington Gardens Conv. Hospital	05-6485	21,999	1,134	579	9,103	7,989	159	0	18,964	5,608
Delta Conv. Hospital	55-5354	20,308	2,457	807	3,745	7,900	298	151	15,358	5,607
El Dorado Conv. Hospital	05-6243	34,710	8,121	2,048	7,904	4,847	2,723	2,702	28,345	20,017
Empress Conv. Hospital	05-6026	70,741	30,480	1,386	19,450	4,004	4,407	2,702	62,429	26,590
Foothill Oaks Care Center	55-5219	49,424	12,079	2,048	15,453	3,937	3,037	315	36,869	29,164
Grass Valley Conv. Hospital	05-5512	76,653	43,516	1,220	14,068	3,393	3,477	243	65,917	13,470
Heritage Conv. Hospital	05-6073	47,682	7,371	2,048	10,071	8,663	2,749	2,790	33,692	29,502
Hilltop Manor Conv. Hospital	05-5776	318,470	222,545	4,241	21,305	14,999	3,805	76	266,971	156,583
Katherine Conv. Hospital	05-5311	42,049	3,333	1,055	14,033	11,369	189	0	29,979	21,193
Lakeport Skilled Nursing Center	05-5499	101,106	2,571	1,862	62,345	3,990	3,938	0	74,706	52,515
Linwood Gardens Conv. Hospital	55-5125	48,433	4,490	2,027	16,328	13,680	523	95	37,143	7,665
Meadow View Manor	55-5283	89,096	42,775	2,048	18,648	1,832	3,587	400	69,290	33,683
Medical Center Conv. Hospital	05-6436	58,679	25,961	2,048	13,838	5,932	1,630	0	49,409	20,525
Mid-Wilshire Conv. Hospital	05-6174	120,260	95,770	1,572	10,267	5,064	1,045	101	113,819	59,967
Montclair Manor Conv. Hospital	05-5718	38,569	3,057	1,220	13,936	10,118	1,240	840	30,411	16,997
Monterey Pines SNF	05-6437	67,189	17,086	2,048	19,057	8,857	1,563	2,702	51,313	34,590
Napa Nursing Center	55-5161	113,307	52,690	2,689	26,100	5,456	4,839	2,702	94,476	42,207
Parkview Nursing Center	55-5058	38,302	5,527	2,048	10,820	8,273	480	2,702	29,850	11,886
Placerville Pines Conv. Hospital	05-5497	24,325	2,582	2,048	5,657	1,951	1,992	1,351	15,581	12,487
River Valley Nursing Center	55-5038	59,676	5,461	2,503	15,803	3,507	4,319	2,719	34,312	29,142
Roseville Conv. Hospital	05-5886	270,707	144,426	4,344	35,503	18,640	4,355	2,831	210,099	157,804
Sacramento Conv. Hospital	55-5122	52,164	14,241	1,779	12,926	6,985	1,452	0	37,383	29,966
Sierra Health Care Conv. Hospital	05-5681	127,888	34,924	2,731	34,905	22,179	1,603	150	96,492	75,330
Sierra Solano Care Center	05-5189	43,327	5,828	1,862	15,125	7,645	1,785	0	32,245	21,152
South Gate Care Center	05-6458	21,378	2,240	2,048	8,926	3,648	1,638	0	18,500	8,580
Sunny Hills Conv. Hospital	05-6151	177,837	36,309	2,048	86,129	30,097	1,543	2,702	158,828	25,540
Vallejo Conv. Hospital	05-5614	49,380	1,808	2,048	13,124	12,381	292	0	29,653	21,641
Valley View Skilled Nursing Center	05-5853	32,654	4,151	1,407	9,985	7,284	1,589	60	24,476	17,124
Walnut Whitney Conv. Hospital	05-6410	59,025	17,493	2,606	9,665	6,175	3,905	2,701	42,545	37,589
Wellesley Manor Conv. Hospital	55-5088	55,446	12,196	1,862	16,403	15,725	1,704	0	47,890	23,248
Westgate Gardens Conv. Hospital	55-5208	74,272	3,675	2,896	22,596	27,347	1,906	0	58,420	28,966
Totals		2,405,056	866,297	63,176	593,218	293,867	67,772	31,035	1,915,365	1,076,338



September 24, 1996

Mr. Lawrence Frelot
Regional Inspector General for Audit Services
Department of Health and Human Services
Region IX, Office of Audit Services
50 United Nations Plaza
San Francisco, CA 94102

SUBJECT: A-09-95-00090

Dear Mr. Frelot:

I am in agreement with **the** subject draft audit report with the exception of the \$90,510 labeled as "unsupported costs" per your Exhibit A, identified as our Exhibit 1, enclosed.

In researching this issue I discovered that the majority of these amounts by facility, related to a reclassification year ending closing journal entry that involved moving expenses from certain ancillary items such as oxygen supplies, durable medical equipment, etc., that had recorded losses, to patient medical supplies (account number 810044). The logic for the reclassification related to our decision that if a given ancillary classification sustained a **loss that** it must be an expense coding problem rather **than** a billing problem. Obviously, there would be no invoices under account number 810044 for these **reclassified** amounts. Please see enclosed Exhibit 2 which includes copies of all facility ancillary expense reclassification journal entries. The facilities with unsupported costs over \$5,000 also include back-up for the reclassification journal entries. As you examine Exhibit 2, please note that the majority of facilities balanced to the dollar when you compare Exhibit 1 amounts to the Exhibit 2 reclassified expenses and year end accrual journal entries. Please note that the following facilities had no ancillary reclassification year ending **journal** entries, and therefore are not included in Exhibit 2: Empress, Heritage, Hilltop Manor, Sacramento, Sierra Solano, Sunny Hills, Vallejo, and Walnut Whitney.

I respectfully request that you reconsider the "unsupported costs" identification and include this \$90,510 as "costs misclassified".

I reviewed the year ending June, 1992, and cannot find any ancillary expenses being **reclassified**, apparently year ending June, 1991, is the last time we did that exercise. Please see enclosed Exhibit 3.

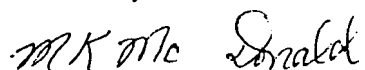
HORIZON WEST HEADQUARTERS, INC.

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Mr. Lawrence Frelot
September 24, 1996
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Thank you for your consideration of my above request, and if you have any questions
please contact me at (916) 624-6230.

Sincerely,

A handwritten signature in cursive script that reads "M K Mc Donald".

M. K. McDonald
Treasurer

Enclosures